



Claire McCaskill
Missouri State Auditor

June 2006

REVENUE

Branch Office Conversion



Office Of
Missouri State Auditor
Claire McCaskill

June 2006

The following findings were included in our audit report on the Department of Revenue, Branch Office Conversion

The Department of Revenue (DOR) incurred unnecessary closing costs that could have been avoided. In April 2002, DOR officials signed a 15 year lease agreement with the Office of Administration (OA) for office space in the Deer Creek Office Building, a privately owned building in the St. Louis area. Since the DOR was closing the office in 2005, it was liable for the lease expenditures until the office was subleased. According to accounting records, the state's General Revenue Fund paid approximately \$39,000 in lease expenditures for vacant office space during the period of May 15, 2005 through October 31, 2005.

The Kansas City branch office closed on June 30, 2005, and was reopened by the contract agent on August 29, 2005, although the contract agent did not sign the OA lease agreement until September 6, 2005. Additionally, the lease agreement prepared by the OA allowed the Kansas City contract agent to make staggered lease payments during the first 12 months of the lease. By allowing the contract agent to stagger lease payments and giving the contract agent a 30-day termination clause, the contract agent could potentially vacate the premises prior to the end of the first year of the lease leaving the state to pursue recovery of lease amounts due.

Four contract agents were allowed to operate without a fully executed contract. Had these agents failed to perform the necessary duties during this time period, the DOR may not have been able to enforce the requirements of the contract agents' agreement. Also, one contract agent did not comply with the contract agreement requirements to register and remain in good standing with the Secretary of State, a misdemeanor. After we informed DOR personnel of the situation, department personnel contacted the agent who then filed his fictitious name registration with the Secretary of State approximately 143 days after the agent's office opened. Additionally, the Kansas City office's contract agent did not submit a business plan until 51 days after the office opened.

The DOR was granted local disposal authority by the Missouri State Agency for Surplus Property (MOSASP) to auction the equipment at the 11 former branch offices. Bids accepted for the equipment ranged from \$151 to \$3,100 for a total of \$16,477 for all 11 offices. Notification of the sealed bid auction was sent to all 182 contract agents operating at that time, as DOR officials determined that other individuals would not be interested in this "worthless equipment". The DOR did not allow an equal opportunity for everyone to inspect the equipment prior to making a bid; however, the 11 contract agents were allowed to inspect the equipment and, in most cases, use the equipment for

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several months. This does not appear to provide a fair, open, and competitive environment for all potential bidders. Furthermore, the auction of state-owned branch office assets included computer equipment and software, printers, televisions, and fax machines which did not appear to meet the MOSASP criteria for condemned property. Based on our review, it appears that the items sold through local disposal should have been transferred to the MOSASP for auction.

The DOR could not account for the disposition of approximately 250 state-owned assets. These 250 items included a laser printer, a fax machine, computers, software, and other miscellaneous items.

The former branch offices are higher volume offices. According to DOR records, during fiscal year 2004, these former branch offices remitted transaction processing fees to the state in excess of \$6.2 million. It appears appointed agents should possess qualities such as experience, knowledge, and business skills that will allow them to successfully achieve their assigned duties in an efficient and effective manner and ensure that Missouri taxpayers receive the level of service they demand. In addition, the DOR should also consider soliciting proposals prior to appointing fee agents. It should be noted that the method used by the current administration to appoint or select contract agents has been a long-standing practice within state government.

The division's goal is to visit each contract agent's office once each month; however, without additional staff, the DOR may not be able to reach this goal. The DOR has only approximately 10 staff positions allocated to monitor the state's 183 contract offices. As of October 25, 2005, the DOR had only performed two monitoring visits of the 11 converted offices.

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DEPARTMENT OF REVENUE
BRANCH OFFICE CONVERSION

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STATE AUDITOR'S REPORT



CLAIRE C. McCASKILL
Missouri State Auditor

Honorable Matt Blunt, Governor
and
Trish Vincent, Director
Department of Revenue
and
Michael N. Keathley, Commissioner
Office of Administration
Jefferson City, MO 65102

We have audited the Department of Revenue's Branch Office Conversion. The scope of this audit included, but was not necessarily limited to, the conversion of 11 state-operated branch offices to contract offices during calendar year 2005. This audit did not review the operations of the other 171 contract offices that existed at the time of our audit. The objectives of this audit were to:

1. Review the conversion of branch offices to contract offices and the related controls over significant management and financial functions.
2. Determine the extent of the conversion process and the related costs of converting branch offices to contract offices.
3. Identify the various accountability and compliance issues relating to the conversion of branch offices to contract offices.

Our methodology to accomplish these objectives included reviewing written policies, financial records, and other pertinent documents as permitted by the department; interviewing various personnel of the Department of Revenue, as well as certain external parties; and testing selected transactions.

Our audit was conducted in accordance with applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and included such procedures as we considered necessary in the circumstances.

The accompanying History and Organization is presented for informational purposes. This information was obtained from the department's management and was not subjected to the procedures applied in the audit of the Department of Revenue's Branch Office Conversion.

The accompanying Management Advisory Report presents our findings arising from our audit of the Department of Revenue's Branch Office Conversion.

A handwritten signature in black ink, reading "Claire McCaskill". The signature is fluid and cursive, with the first name "Claire" and last name "McCaskill" clearly distinguishable.

Claire McCaskill
State Auditor

December 16, 2005 (fieldwork completion date)

The following auditors participated in the preparation of this report:

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MANAGEMENT ADVISORY REPORT -
STATE AUDITOR'S FINDINGS

DEPARTMENT OF REVENUE
BRANCH OFFICE CONVERSION
MANAGEMENT ADVISORY REPORT -
STATE AUDITOR'S FINDINGS

1.	Leases
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The Department of Revenue (DOR) did not adequately plan for the closing of the Deer Creek offices and incurred approximately \$39,000 in lease expenditures for a vacant office. Additionally, the Office of Administration (OA) did not prepare a lease agreement with the Kansas City Office agent in a timely manner, and staggered the lease payments for the Kansas City agent during the first 12 months of the lease term.

Pursuant to the Governor's recommendation, during calendar year 2005 the DOR prepared to close eleven state-operated motor vehicle branch office locations and reopen these offices with contract agents. Many of these offices reopened in the same locations that were previously occupied by the state-operated branch offices.

A review of the lease agreements executed by the state noted the following issues:

- A. By failing to adequately plan the reopening of these offices, the DOR incurred unnecessary closing costs of approximately \$39,000 that could have potentially been avoided. In April 2002, DOR officials signed an agreement with the OA indicating their intent to occupy 7,385 square feet of office space in the Deer Creek Office Building until the lease agreement expired in 2017. This building is a privately owned office building, located in St. Louis.

Since the DOR was closing the office, it was liable for the lease expenditures until the office was subleased. On May 23, 2005, the OA executed a sublease agreement with the contract agent appointed to run the Deer Creek office. According to the sublease agreement, the contract agent agreed to sublease 2,999 square feet of an available 7,385 square feet. The sublease agreement was for the period of May 16, 2005 through June 30, 2005, allowing a month to month lease after June 30, 2005. The contract agent operated from this specific office until August 31, 2005, when the agent moved to a different office within the same building.

On September 1, 2005, the Department of Economic Development filled 2,999 square feet of the available state-leased office space and later filled the remaining portion of the office on November 1, 2005. According to accounting records, the state's General Revenue Fund paid approximately \$39,000 in lease expenditures for vacant office space during the period of May 15, 2005, through October 31, 2005.

- B. Although the Kansas City contract agent began operations on August 29, 2005, the contract agent did not sign the OA lease agreement until September 6, 2005. The Kansas City branch office closed on June 30, 2005, and was reopened by the contract agent on August 29, 2005. As a result, the contract agent was allowed to operate in a state office building without a lease agreement for approximately 6 days. It should also be noted that the lease agreement indicated that the lease was effective on September 1, 2005, despite the fact the agent began office operations on August 29, 2005.

By failing to adequately complete the lease agreement, the OA allowed a contractor to perform business in a state building without having a lease agreement. In the future, the OA should prohibit allowing tenants to move into an office without having a signed lease agreement.

- C. The lease agreement prepared by the OA allowed the Kansas City contract agent to make staggered lease payments during the first 12 months of the lease. The lease allowed the contract agent to pay approximately 25 percent of the annual rent during the first six months of the lease and approximately 75 percent of the lease during the remaining six months of the year. By allowing the contract agent to stagger lease payments and giving the contract agent a 30-day termination clause, the contract agent could potentially vacate the premises prior to the end of the first year of the lease leaving the state to pursue recovery of all applicable lease amounts due.

Additionally, while reviewing a memo prepared by the Kansas City contract agent, we noted that the lease and contract signed by the contract agent was contingent upon the contract agent being the successful bidder of the DOR equipment presently in the state-operated branch office that was being closed. Based on this information, had the contract agent not been the successful bidder on the equipment, it appears the lease and the contract could have been nullified. The contract agent did acquire the equipment in the state run office for \$151 (See MAR No. 3).

WE RECOMMEND the:

- A. DOR adequately plan future state-operated office closings and make every effort possible to reduce the costs to the state's General Revenue Fund of closing offices.
- B. OA ensure that lease agreements are signed by the tenants prior to the time period of the lease.
- C. OA establish policies and procedures to prohibit the staggering of lease payments on future lease agreements.

AUDITEE'S RESPONSE

The Director of Revenue provided the following responses:

- A. *The DOR agrees with the State Auditor that office closings should be adequately planned and related state costs should be minimized. However, the DOR strongly disagrees with the Auditor's conclusion that the branch office conversion process was not "adequately planned." To the contrary, the conversion properly balanced the needs to sustain customer service, provide career counseling and transition time for affected employees, and safeguard tax dollars.*

To explain the competing interests, some context is necessary. On January 26, 2005, Governor Blunt released his FY 2006 budget. That budget included significant changes to the DOR due to voter approval of Amendment 3 in November 2004. The Governor announced \$7.2 million in redirected highway funding and a reduction in the state workforce of 194 positions, by closing eleven DOR motor vehicle and driver licensing branch offices no later than June 30, 2005. This was an absolute deadline because no FY 2006 funds would be available for the branch offices.

Based on the significant loss of highway funding, the DOR responded to the Governor by developing a plan to transition the eleven branch offices to privately operated contract offices during May and June 2005. The DOR's two priorities were to maintain customer service by keeping closing times to a minimum and to safeguard taxpayer dollars.

The first branch office to close was Columbia, on April 29, 2005. The office closed on a Friday and reopened the following Monday, resulting in no lost days of service to customers. Ten of the eleven offices were transitioned with no more than the four business days of being closed (the exception was Kansas City).

The DOR is extremely proud of the conversion process, including the planning to convert eleven offices in less than six months and to follow through on our commitment and dedication to excellent customer service.

The focus on lease payments at Deer Creek misses the point. The underlying Deer Creek lease, entered into in 2002 by the Holden Administration, has often been cited as a poor deal for the state. The rental rate, the amount of space, and the provision that the DOR was to be liable until a subtenant could be located were ill advised.

Having been saddled with this lease, the DOR properly emphasized customer service by downsizing the space needs. If your conclusion that the state spent \$39,000 for vacant space is correct (and we neither confirm nor dispute it), the reason is the 2002 lease, not the 2005 conversion.

- B. *OA agrees with the Auditor that, in a perfect world, leases would be signed before the lease period. In this case, the exigencies of customer service were deemed more important. The six-day time period caused no loss to the state.*

- C. *OA will consider establishing policies as recommended. In this case, the staggered lease was warranted to account for certain start-up costs for the contract agent and to promote customer service.*

AUDITOR'S COMMENT

- A. The state did not pay \$39,000 for vacant leased office space because of a lease approved in 2002. These costs were incurred because this space was vacated in haste, without a cohesive plan to promptly re-occupy the space by another state agency. In addition, we do not understand how downsizing the office space used to serve customers in this high volume office by 60 percent can be characterized as emphasizing customer service.

2. Business Practices

DOR officials allowed four contract agents to operate offices without having a completed contract agreement. In addition, the DOR allowed one agent to operate his office without having registered with the Secretary of State. Also, one contract agent did not submit his business plan within the time frame required by the contract agent agreement.

All contract agents were required to sign a contract prepared by the DOR, which set forth guidelines and requirements that each contract agent was required to follow. A review of the contract and the steps taken to ensure compliance noted the following concerns:

- A. Four contract agents were allowed to operate without a contract signed by both the contract agent and the DOR. We noted a range of 1 to 21 days where these agents were allowed to operate without a fully approved contract. Had these agents failed to perform the necessary duties during this time period, the DOR may not have been able to enforce the requirements of the contract agents' agreement.

The failure by the DOR to obtain completely signed contracts prior to authorizing the contract agents to open their offices exposed the DOR to unnecessary risks. The DOR should prohibit this practice in the future, and only authorize contract agents to open their offices after all required signatures have been obtained.

- B. One contract agent did not comply with the contract agreement requirements to register and remain in good standing with the Secretary of State. After we informed DOR personnel of the situation, the department personnel contacted the agent who then filed his fictitious name registration, with the Secretary of State on October 26, 2005, approximately 143 days after the agent's office opened.

According to Section 417.230, RSMo, any person who engages in or transacts any business in the state of Missouri under a fictitious name without registering, shall be deemed guilty of a misdemeanor. The DOR should ensure all contract agents

are properly registered to do business in the state prior to authorizing them to operate as an agent of the state.

- C. Each contract agent was required by the contract agent agreement to prepare and submit a business plan in a format prescribed by the Director of Revenue within 24 days of appointment. According to DOR officials, the purpose of the business plan was to give the DOR an idea of the management style and proposed operations that each contract agent would apply to their office.

The Kansas City office's contract agent's appointment date was September 20, 2005, which was 23 days after the agent began operations on August 29, 2005. A review of the business plans noted that this contract agent did not submit a business plan until October 19, 2005. While this is only 4 days after the contract due date of October 15, 2005, it was 51 days after the office opened.

By failing to submit a business plan, the DOR was unaware of the goals and business practices that would be used by the newly appointed agent until almost two months after the agent began operations. In addition, to fully utilize the value of business plans, the plans should be submitted by the potential agents prior to the selection of the contract agents.

- D. Electronic telephone answering services at two contract agent offices did not provide an option to speak with office personnel. According to the contract agreement, if the contract agent uses an electronic telephone answering service, such service must provide the option to speak with office personnel. If office personnel are not available to take the call, an option must be provided to leave a message that will be responded to no later than the next business day.

By not fully monitoring the contract agents, the DOR has not ensured that all customer service provisions have been met. It is important that taxpayers be able to ask questions of office personnel to ensure their motor vehicle transactions can be completed in a timely and efficient manner. The DOR should ensure that the level of service provided by each contract agent complies with the contract agent agreement.

WE RECOMMEND the DOR:

- A. Ensure contract agreements are signed by all necessary parties prior to the time the contract becomes effective.
- B. Ensure each contract agent is registered with the Secretary of State prior to conducting business, as required by state law.
- C&D. Ensure each contract agent complies with all of the requirements of the contract agent agreement.

AUDITEE'S RESPONSE

The Director of Revenue provided the following responses:

- A. *While the Auditor correctly reported that four offices opened prior to the contract being signed by all parties, the Columbia office agent, as noted below, signed the formal contract prior to opening. All four agents received tentative appointment letters signed by the Director of Revenue prior to opening for business. All four agents had copies of the contract and had voiced no major concerns. The table below identifies the specific offices and illustrates relevant timeframes:*

<i>Office</i>	<i>Date of Tentative Appointment Letter</i>	<i>Formal Contract Signed By</i>		<i>Open Date</i>
		<i>Agent</i>	<i>Director of Revenue</i>	
<i>Columbia</i>	<i>4/11/05</i>	<i>4/29/05</i>	<i>5/3/05</i>	<i>5/2/05</i>
<i>Deer Creek</i>	<i>4/28/05</i>	<i>5/17/05</i>	<i>5/25/05</i>	<i>5/16/05</i>
<i>South Kingshighway</i>	<i>4/20/05</i>	<i>6/27/05</i>	<i>6/30/05</i>	<i>6/20/05</i>
<i>Kansas City</i>	<i>8/10/05</i>	<i>9/7/05</i>	<i>9/20/05</i>	<i>8/29/05</i>

The DOR agrees that, in a perfect world, formal contracts should be signed prior to their effective dates. We are also aware this is not always possible. In this case, given the necessity for turning offices around in record time to maintain customer service, the DOR is comfortable with its process. To the extent the report would have us keep an office closed where the agent has a tentative appointment letter and has received a contract for review and indicated no issue with it, we simply disagree. In such circumstances, the taxpayers are better served by opening the office rather than awaiting contract signature.

- B. *The DOR concurs with the Auditor's recommendation.*

C&D. *The DOR concurs with the Auditor's recommendation.*

As noted, one purpose of the business plan is to give the DOR an idea of the management style and proposed operations that each contract agent would apply to their office. An additional purpose is to structure the agent-DOR relationship in a manner similar to any business relationship. The business plan concept was developed by the current administration to clearly communicate what Missouri taxpayers can reasonably expect in terms of service levels from the contract agents. No contract agent was ever required to submit a business plan before January 2005. It is true the Kansas City business plan was submitted later than it should have been. Nonetheless, this created no negative impact on the DOR, our customers, or the taxpayers.

Related to the concern noted by the Auditor in reference to electronic telephone answering services, the DOR has worked with the Independence and North Kingshighway offices upon identification of the answering service concern. We note that this contractual requirement was also initially stipulated by the current administration.

3.**Sale of Equipment**

The DOR did not comply with policies and procedures issued by the Missouri State Agency for Surplus Property (MOSASP). The DOR did not solicit bids for surplus equipment in an open and competitive environment, and did not accurately prepare reports of state-owned surplus property, commonly referred to as the SS-1 forms. Additionally, the DOR did not follow procedures for depositing the proceeds from the sale of equipment as required by MOSASP policies and procedures.

In conjunction with the closing of 11 state-owned branch offices located throughout the state, the DOR was granted local disposal authority by the MOSASP to auction the equipment maintained at these former locations. The following chart indicates the bids accepted for the equipment sold by the DOR:

Bidder	Amount
Columbia Agent	\$ 2,125
Deer Creek Agent	2,800
Independence Agent	803
Jefferson City Agent	1,022
Joplin Agent	360
North Kingshighway Agent	1,500
Raytown Agent	707
St. Joseph Agent	1,509
South Kingshighway Agent	2,400
Springfield Agent	3,100
Kansas City Agent	151
Total	\$ <u>16,477</u>

A review of the auction and supporting documentation noted the following concerns:

- A.1. Based on the review of the invitation for bid, it appears the opportunity for bidding on the equipment was not handled on a truly competitive basis since it did not allow an equal opportunity for everyone to inspect the equipment prior to making a bid. On July 8, 2005, the DOR was granted local disposal authority by the MOSASP for the equipment that was maintained in the state-owned motor vehicle and driver's license branch offices located throughout the state. The DOR eventually sold the state-owned branch office equipment through a sealed bid auction, with notification of the invitation to bid being sent to all 182 contract agents operating at that time in the state.

The DOR issued an invitation on July 25, 2005, to bid on the state-owned equipment maintained at the former branch offices. According to the DOR, the target audience for these assets was all contract agents throughout the state. DOR

officials determined that other individuals would not be interested in this "worthless equipment". Although contract agents were informed of the invitation to bid on this equipment, the DOR did not allow any inspection periods for the agents to view the condition of the equipment.

While not allowing an inspection period for all contract agents, the 11 contract agents were allowed to inspect the equipment and, in most cases, use the equipment for several months prior to the invitations to bid being issued. Allowing the 11 newly appointed contract agents the advantages of both viewing and using the equipment did not appear to provide a fair, open, and competitive environment for all potential bidders. Since these 11 agents were allowed to use the equipment, they knew the condition of the equipment and were in an advantageous position to determine the equipment's capabilities and value. The following table indicates the number of days each fee agent was allowed to use equipment prior to submitting the winning bid.

Office Location	Closing Date	Reopen Date	Date bids awarded	Number of days equipment remained in the fee agents possession
Jefferson City	6/15/2005	6/20/2005	8/8/2005	48
St. Joseph	6/15/2005	6/20/2005	8/8/2005	48
Kansas City	6/15/2005	8/29/2005	8/22/2005	(7)
South Kingshighway	6/15/2005	6/20/2005	8/8/2005	48
North Kingshighway	6/15/2005	7/20/2005	8/8/2005	18
Columbia	4/29/2005	5/2/2005	8/8/2005	96
Deer Creek	5/13/2005	5/16/2005	8/8/2005	82
Springfield	5/13/2005	5/16/2005	8/8/2005	82
Joplin	5/13/2005	5/16/2005	8/8/2005	82
Independence	5/13/2005	6/6/2005	8/8/2005	62
Raytown	5/13/2005	6/3/2005	8/8/2005	65

Out of the approximately 182 agents given the opportunity to bid on the equipment, only 12 agents (less than 7 percent) submitted a bid for these assets. Of the twelve bids received only one bid was from an agent that did not receive a former branch office location, indicating that the true target audience was most likely the agents appointed to run the 11 former branch offices. By the end of August 2005, all equipment offered for sale from the 11 former branch offices had been sold to the new contract agents for a total of \$16,477. Since the 11 new contract agents had been using and relying on the equipment to conduct business, had the new contract agent not been awarded the bids to purchase the equipment the operations of the agents' offices may have been significantly impacted.

Allowing a portion of the target audience to use the equipment during the auction while the remaining potential bidders could not inspect the equipment created an unfair advantage. Also, by limiting the potential market for this property, the DOR may have reduced the proceeds from the sale of the surplus property. In the future, the DOR should ensure the equipment being identified is of little or no value before requesting local disposal. If MOSASP authorizes local disposition the DOR should establish procedures to conduct an auction in such a manner to ensure fairness to all potential bidders.

A.2. According to the MOSASP policies and procedures, departments may request local disposal authority for items the department considers to have little or no transfer or sale value. MOSASP policies and procedures also indicate the items that should be considered for local disposal, which include, condemned wood furniture; broken, torn, or wet stuffed couches and chairs; mattresses; potentially hazardous material; used tires; batteries; condemned appliances; computer "dummy" terminals, etc.. The auction of the state-owned branch office assets included computer equipment and software, printers, televisions, and fax machines which did not appear to fit the criteria for condemned property. According to DOR records, the purchase price of the items that were auctioned was approximately \$209,750 and the book value was approximately \$2,375, which does not include items less than \$1,000 or items not considered to be sensitive. The DOR auction of these items generated proceeds of approximately \$16,477. Based on our review, it appears that the items sold through local disposal should not have been considered condemned property by the DOR and should have been transferred to the MOSASP for auction.

B. The DOR deposited all proceeds from the sale of the former branch office fixed assets into the State Highway and Transportation Department Fund. A portion of the proceeds should have been deposited into the state's General Revenue Fund and the department's federal fund. MOSASP policies and procedures require a state agency to complete a separate report of state-owned surplus property for each funding source of the surplus equipment. The funding source of the equipment is defined as the fund that was originally used to purchase the equipment.

The forms filed with MOSASP noted the funding source for all of the equipment as the State Highway and Transportation Department Fund. However, our tests of 100 items listed on the report of state-owned surplus property found that only 62 of these items were actually purchased from the State Highway and Transportation Department Fund. The remaining 38 items were originally purchased with funding from the state's General Revenue Fund and the DOR's federal fund.

The DOR should determine the amounts due to each fund and request the OA to make the appropriate transfers to return the sales proceeds to the proper funds. In addition, the DOR officials should review the sale of federal property to

determine whether this sale was conducted in accordance with federal guidelines and the proper disposition of the sale proceeds of this equipment. Property purchased with federal funds must be disposed of in accordance with federal guidelines.

WE RECOMMEND the DOR:

- A. Comply with state surplus property policies and procedures. Furthermore, any future sales of surplus property should be offered to the public in a fair and competitive manner.
- B. Request transfers be made to ensure the proceeds from the sale of surplus property are deposited into the correct fund. In addition, the DOR should review the federal guidelines regarding property dispositions to ensure it has complied with them.

AUDITEE'S RESPONSE

The Director of Revenue provided the following responses:

- A. *The DOR could not disagree more strongly with the conclusions in Section 3.A. The total book value (calculated by SAMII) of the hundreds of items bid was \$2,375.32. The average purchase date was 1996. For that essentially worthless equipment, our bidding process obtained payments of \$16,476.99. The net "profit" to the state was \$14,101.67. Any business owner would be ecstatic at such a return, and so are we.*

The report wrongly concludes that "[t]he DOR did not comply with policies and procedures issued by the Missouri State Agency for Surplus Property (MOSASP)." On July 8, 2005, MOSASP granted the DOR local disposal authority for all equipment in the eleven branch offices. On July 13, OA advised the DOR to either throw the equipment away or try to obtain three bids - the choice was ours, and OA instructed us to do what was in the best interest of the citizens. I want to emphasize that the instruction was to try to obtain three bids, but there was no requirement that we do so. Based on that authority, the DOR engaged in a detailed analysis of the property. First, we designated all equipment of value to us for return. The net book value of that equipment was \$15,690.85. That equipment was returned and is being used today. Second, as to the equipment we had no use for, we determined that disposing of it would cost about \$44,000 in General Revenue dollars. Not wanting to incur that expense and hoping to obtain some return for the equipment, we made the equipment available for bid by all contract offices. In some cases multiple bids were received, in some cases only one. As noted above, that process was a resounding success for the state - we were paid \$16,476.99 for equipment worth \$2,375.32. Any suggestion that obtaining more bids would have netted more money is simply speculation.

The report criticizes us for not allowing inspection of the equipment, for advertising the process to only contract agents, and for permitting agents who took over the state offices to use the equipment in the interim.

We disagree with each point. The results undercut any suggestion that a more extensive inspection and bidding process might have resulted in a better result. It simply makes no sense to engage in a lengthy and formal inspection and bidding process for hundreds of items of condemned property with book value of less than \$2,500, with an average age of nine years.

Moreover, the report gives no weight to the costs of such a process. We would have had to pay costs to store equipment and advertise it, and pay personnel to conduct the inspection and bidding you suggest. The equipment was in use in the branch offices until they closed. Should we have kept offices closed for, say, two weeks, to permit inspection? Or perhaps inconvenience Missouri citizens by making them wait for service while some potential bidder inspected a 10-year old printer? Such a process is neither mandated by law nor desirable.

We also disagree with the conclusion that we should not have allowed the contract agents to temporarily use the equipment. As we have stressed, the turnaround time on ten of the eleven offices was four business days or less. Permitting temporary use of the equipment promoted that turnaround, and gave Missouri's citizens better service from the minute the contract offices reopened. We stand by our decision to permit such use.

The bottom line on this point is that we followed the letter of the law and obtained a great result for Missourians by limiting office closing times, obtaining a significant profit on the equipment we sold, and avoiding the costs of an elaborate and unnecessary bid process. We are proud to stand on that record.

- B. *Due to the nature of the branch office operations, the DOR determined that depositing the sale proceeds to the highway fund was appropriate. The vast majority of the equipment was purchased with highway dollars, because highway dollars funded the vast majority of branch office operations. It might be true that some pieces of equipment were purchased by General Revenue dollars. Given the small amount of dollars at stake, we decided that the value of the time associated with analyzing the funding source of the hundreds of items sold does not justify the cost in terms of potential benefit to the General Revenue Fund. Related to items initially purchased with federal funds, the DOR will research and make transfer requests as deemed necessary.*

AUDITOR'S COMMENT

- A. Nearly all aspects of the manner in which this state-owned equipment was handled and disposed of as a result of the closing of the branch offices was contrary to the basic principles of how government should be conducting business. Regardless of what the DOR claims, the initial give-away and later sale of this state-owned equipment was conducted in a vacuum. Our attempts throughout the conversion plan and process to

obtain information and to verify the state-owned equipment involved in these conversions were met with extreme resistance and a total lack of cooperation by the DOR. This **usable** state-owned equipment was intended for a chosen few and the manner in which this government business was conducted is a clear example of **preferential treatment**. Our comments and recommendations noted above are fully supported by the facts presented.

- B. It appears the department chose to ignore its own records and dispose of the sale proceeds in a manner they assumed was appropriate. Using the department's records, we determined the fund ownership of this property with relative ease. While the department is researching its records to make the proper transfers to federal funds, it should be a simple task to do the same for amounts due to the state's General Revenue Fund.

4. Capital Asset Records

The DOR does not have accurate and complete capital asset records and could not account for the disposition of approximately 250 state-owned assets.

In August 2005, we received a fixed asset listing from DOR officials. We compared the listing of assets assigned to the former branch offices to listings of items sold through an auction, transferred, or disposed. This comparison identified approximately 250 assets listed as former branch office property that appeared to be unaccounted for. These 250 items included a laser printer, a fax machine, computers, software, and other miscellaneous items. These unaccounted for items had an original purchase price of approximately \$360,000 and a book value of approximately \$3,400. Since most of these items could not be located, and were considered lost, stolen or missing, the department removed them from their fixed asset listing.

A second capital asset listing received from department officials in December 2005 indicated that approximately 90 assets were still maintained by the branch offices although these offices had been closed at least six months earlier. DOR officials identified these assets as items that were either locally disposed of by the former branch offices, missing items, or possibly stolen items. These items had an original purchase price of approximately \$111,800 and a book value of approximately \$3,365. The DOR conducted a physical inventory in July 2005, and noted that approximately 90 items were not located. Despite the fact that these items cannot be located, these items remain on the DOR fixed asset listing.

Failure to maintain accurate capital asset records or to properly account for state-owned property increases the likelihood that assets may be lost, stolen, or incorrectly valued. Property records should be maintained on a perpetual basis, accounting for property acquisitions, dispositions, and other changes as they occur. According to 15 CSR 40-2.031 (9), state agencies are required to perform physical inventories annually and reconcile the physical inventory to property control records. Physical inventories are necessary to ensure the capital asset records are accurate, identify any unrecorded

additions and deletions, detect theft of assets, and identify obsolete assets. Complete and accurate records of state-owned property are necessary to provide adequate control over public property.

WE RECOMMEND the DOR should establish procedures to ensure that the information derived from a physical inventory is updated to the fixed asset records in a timely manner as required by 15 CSR 40-2.031 (9). Also, the DOR should follow-up on the unaccounted for property items, as well as any discrepancies noted during future inventories.

AUDITEE'S RESPONSE

The Director of Revenue provided the following response:

The DOR had and continues to have established procedures that comply with 15 CSR 40-2.031. Every effort will be made to account for these items with a book value of \$3,367.54, or an average of \$38 each, prior to authorizing them for deletion from fixed asset records.

5. Selection and Oversight of Contract Agents
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The DOR has not established criteria or solicited proposals for selection of contract agents. As a result, there is no assurance the contract agents who would provide the best quality of service to Missouri taxpayers have been selected. It should be noted that the method used by the current administration to appoint or select contract agents has been a long-standing practice within state government. In addition, the DOR may not be able to adequately monitor all contract agents with current resources.

- A. The former branch offices that were privatized are higher volume offices, and thus processed more transactions than other license offices throughout the state. According to DOR records, during fiscal year 2004, the former branch offices remitted transaction processing fees to the state in excess of \$6.2 million. To ensure that Missouri taxpayers receive the level of service they are accustomed to, it appears that the appointed contract agents should be held to standards other than just their political affiliation. Appointed agents should possess qualities such as experience, knowledge, and business skills that will allow them to successfully achieve their assigned duties in an efficient and effective manner.

In addition to establishing criteria to select contract agents, the DOR should also consider soliciting proposals prior to appointing fee agents. By soliciting proposals, the DOR could evaluate and select contract agents that will provide the best service to Missouri taxpayers. The potential items that could be included in a candidate's proposal may include, but not necessarily be limited to, location of the office, available square footage, whether ample parking exists, number of employees (both administrative and clerks) and hours of operation.

The Missouri Supreme Court issued an opinion in Courtway v. Carnahan, No 54402, (Missouri App. W. D., June 23, 1998) indicating that the position of a fee agent is simple and generic and no special skill or professional knowledge was found necessary for appointment. In addition, the Missouri Supreme Court decision also indicated that several individuals would easily qualify for the position with little work in completing the work required. Although the Missouri Supreme Court decision stated almost anyone could be considered as a candidate for the contract agent appointment, appointing a candidate that has no prior experience or knowledge, or the ability to run an office, could reduce the level of service provided to Missouri taxpayers.

Since no knowledge or skill requirements have been established, the level of service provided to Missouri taxpayers may be at risk. By soliciting proposals and establishing requirements, the DOR could better address the needs of Missouri taxpayers, and potentially offer a higher quality of service. In addition, the DOR should support any legislation requiring the contract agents to be selected through a competitive process.

- B. The DOR may not have adequate resources to thoroughly and effectively monitor the 11 converted high volume offices and the other 172 offices that are currently operated by contract agents. As of October 25, 2005, the DOR had only performed two monitoring visits of the 11 converted offices. Additionally, the DOR has only approximately 10 staff positions allocated to currently monitor the state's 183 contract offices.

In our prior report on the DOR, Division of Motor Vehicle and Drivers Licensing, we identified several concerns regarding procedures over transaction processing and documentation, monitoring of office operations, accountability and accuracy of collections, and controls over items issued to and sold by the field offices. At the time of our prior report, the department noted that staff reductions were being made in the division and these reductions have continued, leaving only 10 positions in the division's Customer Assistance Bureau to monitor the current 183 contract fee agent offices that now exist. The division's goal is to visit each contract agent's office once each month; however, without additional staff, the DOR may not be able to reach this goal.

Because of the volume and variety of transactions that are processed by the fee agents, the amount of state funds that are collected by the agents, and the risks associated with these offices, it is imperative that the DOR have an effective, timely, and thorough monitoring system in place. The DOR should request additional resources to ensure that contract agents are adequately monitored within the established goals. Since contract agents handle large quantities of cash, the failure to adequately monitor contract agent exposes the state to the potential to lose revenue and reduces the quality of services being provided to the taxpayers.

WE RECOMMEND the DOR:

- A. Consider establishing minimum experience and educational requirements for potential candidates. In addition, the DOR should consider soliciting proposals to maintain an acceptable level of service and support legislation that requires contract agents to be selected through a competitive evaluation process.
- B. Ensure resources are available to adequately and effectively monitor the operations of all of the state's contract fee agents.

AUDITEE'S RESPONSE

The Director of Revenue provided the following responses:

- A. *While we do not necessarily disagree with this conclusion, we do not feel it is in proper context, nor is it within the auditor's authority or competence to make.*

First, some context. The report concludes that, "the appointed contract agents should be held to standards other than just their political affiliation" and "should possess qualities such as experience, knowledge, and business skills." This Administration has done just this, to a degree unprecedented in Missouri history. There are 38 non-profit entities that serve as contract agents, a record high number. All agents must submit and adhere to a business plan - just the tool to show "experience, knowledge, and business skills." Until January 2005, no contract agent was ever required to submit a business plan. We have announced plans to competitively bid the next open office as a pilot - again something that no other Administration has done. Finally, I note that the Auditor's Office made no such recommendations from January 1999 until now.

Second, as to the law. The report cites the Courtway v. Carnahan decision, which leaves the selection of contract agents to the Governor and the DOR, with no role for the Auditor. It specifically holds that political affiliation is an appropriate requirement for operating a contract office. The report's conclusion to the opposite is contrary to established law. Further, it does not appear to me that this recommendation meets Standard 2.09 of the Comptroller General's Government Auditing Standards (2003). That standard requires that a performance audit

entail an objective and systematic examination of evidence to provide an independent assessment of the performance and management of a program against objective criteria as well as assessments that provide a prospective focus or that synthesize information on best practices or cross-cutting issues.

The examination was not systematic, nor did it weigh our work against objective criteria. Indeed, the best "objective criteria" is controlling law, which is contradicted. Finally, one must question the objectivity and independence of the examination since the Auditor's Office had six years to make recommendations about contract agent selection while your party was in power, but failed to do so.

- B. *Independent of this audit, the DOR has reallocated vacant positions, resulting in the number of field coordinator positions increasing from 10 to 14. Each field coordinator is expected to visit each office in his/her designated region at least once per month. During the visit, the coordinator completes and documents an office review, which is designed to take approximately one business day to complete. The review consists of evaluative criteria that will provide the DOR assurance regarding contractual compliance.*

AUDITOR'S COMMENT

- A. The conversion of these 11 high volume branch offices to contracted agents and the manner in which certain aspects of these conversions were handled, as noted throughout this report, indicates a clear need for the state to re-evaluate the processes used to appoint these agents. Also considering the significant amount of the potential profits available to these contract agents, it appears time for the state to reconsider the appropriateness of the patronage system that has long been used to appoint DOR contract agents. Such a recommendation by our office is clearly within our authority and is made in the interests of all taxpayers and in the need to operate state government in an efficient, effective, and public manner. We are pleased the current administration is initiating procedures to follow our recommendation of awarding offices using a competitive process.

HISTORY, ORGANIZATION, AND
STATISTICAL INFORMATION

DEPARTMENT OF REVENUE
BRANCH OFFICE CONVERSION
HISTORY, ORGANIZATION, AND
STATISTICAL INFORMATION

The Department of Revenue was created by Article IV, Section 12, of the Missouri Constitution. The Department of Revenue was given authority and responsibility to collect all monies due to the government of Missouri as provided by law. The Department of Revenue is headed by the director of revenue who is appointed by the governor with the advice and consent of the Senate. The laws governing some of the duties of the director of revenue are set forth in Section 136.030(2), RSMo. This section, in brief, provides that the director of revenue shall make provisions for the collection of motor vehicle registration fees, sales and use tax, motor vehicle trailer, and marine craft in the state, and the licensing of all operators of motor vehicles residing in this state. To accomplish this, the Motor Vehicle Bureau (MVB) was established. The MVB is one of six bureaus under the Customer Services Bureau.

The MVB operations are set forth in Chapters 301, 302, and 306, RSMo. These chapters document the regulations for motor vehicles and marine craft in the state. The Customer Assistance Bureau is responsible for administering the operation of contract offices throughout the state. Pursuant to Section 136.055, RSMo, the director of the Department of Revenue appoints contract agents to act as agents of the department and to operate the contract offices .

Prior to January 2005, there were 171 contract agents and 11 branch offices. These contract agents do not receive a salary from the DOR, but do receive fees from citizens for each transaction performed. The table below summarizes the fees currently collected by each agent for each type of transaction.

Transaction Type	1yr Processing Fee	2 yr Processing Fee
License, renewal, or transfer of registration	\$ 3.50	7.00
Application for Title or transfer of title	2.50	5.00
Driver, operator, or chauffeur's license	5.00	10.00
Notice of lien	\$ 2.50	5.00

The following table indicates the branch offices that were converted to fee offices, the dates the office closed and the dates the office reopened, as well as the estimated processing fees that could potentially be collected by the appointed fee agents. In addition, this table identifies whether the appointed agent remained in the same location that the branch office was located or whether the agent moved the office to a new location.

Office Location	Closing Date	Reopen Date	Estimated Processing Fees*	Same Location	New Location
Columbia	4/29/2005	5/2/2005	\$ 679,200	X	
Deer Creek**	5/13/2005	5/16/2005	609,900	X	
Independence	5/13/2005	6/6/2005	556,700	X	
Jefferson City	6/15/2005	6/20/2005	555,200	X	
Joplin	5/13/2005	5/16/2005	541,800		X
Kansas City	6/15/2005	8/29/2005	409,300	X	
North Kingshighway	6/15/2005	7/20/2005	282,100		X
Raytown	5/13/2005	6/3/2005	589,000	X	
South Kingshighway	6/15/2005	6/20/2005	580,000	X	
Springfield ***	5/13/2005	5/16/2005	975,800	X	X
St. Joseph	6/15/2005	6/20/2005	435,500		X
			<u>\$ 6,214,500</u>		

*- Estimated processing fees are based on the fees collected by the branch offices in FY-2004.

** - Moved into a new office within the same location

***- The Springfield location was split into 3 separate locations, 2 opened in new locations, and 1 remained in the state office building.

Section 32.040, RSMo, provides the director of revenue with the authority to establish and maintain permanent branch offices. In January 2005, the Governor decided to eliminate the 11 branch offices and replace them with contract offices in the same communities.

Trish Vincent is the Director of the Department of Revenue. Julie Allen is the Director of the Customer Services Division and Lynn Bexten is the Administrator of the Customer Assistance Bureau.

An organization chart follows:

DEPARTMENT OF REVENUE
ORGANIZATION CHART
June 30, 2005

